

Message Text

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ACTION EA-09

INFO OCT-01 EUR-12 IO-11 ISO-00 CIAE-00 DODE-00 PM-04 H-02

INR-07 L-03 NSAE-00 NSC-05 PA-02 PRS-01 SP-02 SS-15

USIA-15 AID-05 EB-07 CIEP-02 TRSE-00 STR-04 OMB-01

CEA-01 COME-00 FRB-01 XMB-04 OPIC-06 LAB-04 SIL-01

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R 270617Z FEB 76

FM AMEMBASSY CANBERRA

TO SECSTATE WASHDC 7598

INFO AMCONSUL BRISBANE

USDEL MTN GENEVA

AMEMBASSY LONDON

AMCONSUL MELBOURNE

USMISSION OECD PARIS

AMCONSUL PERTH

AMCONSUL SYDNEY

AMEMBASSY TOKYO

AMEMBASSY WELLINGTON

CINCPAC

UNCLAS SECTION 1 OF 2 CANBERRA 1549

SYDNEY ALSO PASS TRADE CENTER

CINCPAC FOR POLAD

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SUBJ: ECONOMIC PROGRAM OF NEW GOVERNMENT

REF: (A) CANBERRA 718 (NOTAL), (B) CANBERRA 1228 (NOTAL),
(C) CANBERRA 0012 (NOTAL), (D) CANBERRA 0134 (NOTAL),
(E) 75 CANBERRA A-109 (NOTAL)

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QM BEGIN SUMMARY: THE INITIAL ECONOMIC STRATEGY OF THE

LIBERAL/CP GOVERNMENT IS CLEAR ALTHOUGH IMPLEMENTATION IS JUST STARTING. THE OVERALL STRATEGY TO RESTORE EMPLOYMENT AND ECONOMIC ACTIVITY HAS TWO BROAD INTERRELATED THRUSTS, EACH OF WHICH IMPLIES A RANGE OF SPECIAL MEASURES: (1) TO REDUCE AUSTRALIA'S HIGH INFLATION RATE AND (2) TO RESTORE INVESTMENT, BUSINESS ACTIVITY, AND EMPLOYMENT. WHILE SEVERAL CONCRETE STEPS HAVE BEEN TAKEN IN THE TWELVE WEEKS SINCE THE GOVERNMENT TOOK OFFICE, IMPLEMENTATION IS STILL PATCHY AND A MORE RAPID PACE IS LIKELY NOW THAT AUSTRALIA'S SUMMER IS OVER AND PARLIAMENT HAS RECONVENED.

2. INSUFFICIENT TIME HAS PASSED TO PRODUCE MEASURABLE RESULTS FROM ACTION TO DATE. THE LONGER-RUN PROSPECTS, CLOUDED INTERNALLY BY THE INFLATIONARY MOMENTUM AND EXTERNALLY BY WEAKER MARKETS, ESPECIALLY IN JAPAN, SUGGEST A SLOW RATE OF PROGRESS AGAINST INFLATION AND UNEMPLOYMENT. FROM THE U.S. STANDPOINT, NEW GOVERNMENT'S MORE RECEPTIVE ATTITUDE TO FOREIGN INVESTMENT, MINERALS INVESTMENT AND OVERSEAS MINERALS REQUIREMENTS IS ESPECIALLY IMPORTANT. THIS POLICY PROSPECT IS PARTIALLY OFFSET BY THE PROBABILITY OF A MORE PROTECTIVE TRADE POLICY ALTHOUGH PROTECTION IS LIKELY TO FALL ONLY MODERATELY ON AREAS OF DIRECT U.S. EXPORT INTEREST. END SUMMARY.

3. THE NEW GOVERNMENT'S DRIVE TO RESTORE ECONOMIC ACTIVITY COMPRISES TWO INTERRELATED EFFORTS. (1) TO BEAT BACK AUSTRALIA'S CURRENT FOURTEEN PERCENT INFLATION AND (2) TO RESTORE INCENTIVES AND FREEDOM TO BUSINESS INVESTMENT AND EXPANSION.

4. DESPITE THE "CRISIS" TONE OF THE LIBERAL ELECTION CAMPAIGN, THE POST-ELECTION PACE OF CONCRETE ACTION IN THE ECONOMIC AREA HAS BEEN RELATIVELY SLOW. THIS MAY REFLECT IN PART THE FACT THAT IN ITS FINAL DAYS THE ECONOMIC POLICY OF THE WHITLAM GOVERNMENT HAD ALREADY MOVED A LONG DISTANCE IN THE GENERAL DIRECTION OF THE LIBERAL POSITION, AND PARTLY THE DRAG OF THE TRADITIONAL AUSTRALIAN SUMMER VACATION SEASON WITH PARLIAMENT OUT OF SESSION. THE PACE OF ECONOMIC POLICY ACTION WILL PROBABLY QUICKEN IN THE FUTURE.

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TM THE ANTI-INFLATION EFFORT HAS CONCENTRATED TO DATE ON REDUCTION OF EXCESS LIQUIDITY. SPECIAL MEASURES INCLUDE STEPS TO PRUNE GOVERNMENT SPENDING (AND MORE AMBITIOUS STEPS TO THIS END OF FY 1977), AND THE MONETARY PACKAGE (CANBERRA 718) WHICH ADJUSTED INTEREST RATES, MODIFIED BANK LOAN POLICY AND INTRODUCED SPECIAL BOND ISSUES. THE MAGNITUDE OF THE INFLATION PROBLEM ALSO LED THE GOVERNMENT TO AN UNSUCCESSFUL EFFORT TO CUT BACK ON WAGE INDEXATION

WHILE STRONG POLITICAL PRESSURE INDUCED IT TO ABANDON ITS EARLIER INTENTION TO ABOLISH THE PRICES JUSTIFICATION TRIBUNAL. THE GOVERNMENT SUCCESSFULLY RESISTED VARIOUS PRESSURES TO DEVALUE THE A DOL, CITING THE INFLATIONARY IMPACT OF SUCH A MOVE (CANBERRA 0012).

6. MEASURES TO REVIVE INVESTMENT AND BUSINESS ACTIVITY CENTER IN TURN ON (1) A LONG-TERM EFFORT TO TRANSFER RESOURCES FROM THE PUBLIC SECTOR TO THE PRIVATE SECTOR AND (2) EFFORTS TO IMPROVE THE PROFITABILITY OF, AND INCENTIVES FOR, PRIVATE BUSINESS. THE MOST TANGIBLE STEPS TO DATE UNDER THESE HEADINGS HAVE BEEN THE ANNOUNCEMENT OF A 40 PERCENT INVESTMENT ALLOWANCE, A RECEPTIVE ATTITUDE TOWARD FOREIGN INVESTMENT (CANBERRA 0134)(IN THIS CASE A DETAILED MINISTERIAL STATEMENT IS EXPECTED IN COMING WEEKS), AND DEFERRAL OF PAYMENT OF COMPANY INCOME TAXES UNTIL MID 1977. THE GOVERNMENT'S INDICATED WILLINGNESS TO PROTECT IMPORT-SENSITIVE INDUSTRIES ALSO BELONGS IN THIS CATEGORY, ALTHOUGH NO SPECIFIC MEASURE HAVE YET BEEN TAKEN.

7. ONE ECONOMIC STEP OF MAINLY POLITICAL IMPORTANCE WAS THE RESTORATION ON FEBRUARY 10 OF A SUBSIDY (ABOLISHED IN 1974) ON SUPERPHOSPHATE FERTILIZER FOR AGRICULTURAL USE. WHILE THIS MEASURE DOES NOT FIT DIRECTLY INTO THE OVERALL POLICY FRAGK DESCRIBED ABOVE, IT FULFILLS A CAMPAIGN COMMITMENT ESPECIALLY IMPORTANT TO THE COUNTRY PARTY WING OF THE COALITION.

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R 270617Z FEB 76

FM AMEMBASSY CANBERRA
TO SECSTATE WASHDC 7599
INFO AMCONSUL BRISBANE
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8. INSUFFICIENT TIME HAS PASSED TO PERMIT STATISTICAL MEASUREMENT OF THE IMPACT OF THE GOVERNMENT'S ECONOMIC PROGRAM. UNEMPLOYMENT CONTINUED HIGH IN JANUARY WITH SOME DISPUTE OVER THE SIGNIFICANCE OF AN INCREASE IN THE UNADJUSTED UNEMPLOYMENT FIGURE (TO 5.7 PERCENT) AND A DECREASE IN THE SEASONALLY ADJUSTED FIGURE (TO 4.3 PERCENT). FOOD PRICES CONTINUED TO RISE IN JANUARY BUT NO NEW OVERALL CPI PRICE DATA ARE AVAILABLE FOR THE PERIOD SINCE DECEMBER
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31. THE RECENTLY-ANNOUNCED RECORD ONE-MONTH FOOD PRICE INCREASE OF 3 PERCENT IN JANUARY SUGGESTS A SUBSTANTIAL CPI INCREASE WHEN MARCH QUARTER RESULTS ARE ANNOUNCED. A MODERATE EXPORT SURPLUS CONTINUED IN JANUARY. FOLLOWING THE SPECULATIVE RUN WHICH REDUCED RESERVES BY ADOLDS 630 MILLION IN DECEMBER, UNOFFICIAL REPORTS INDICATE A FRACTIONAL RECOVERY OF ABOUT ADOLDS 150 MILLION IN JANUARY. DESPITE VIGOROUS PRUNING OF GOVERNMENT EXPENDITURE, THE PROSPECT IS THE THE FY1976 FEDERAL GOVERNMENT DEFICIT WILL STILL EXCEED ADOLDS 4 BILLION, THEREBY COMPLICATING THE EFFORT TO CURB LIQUIDITY. LESS TANGIBLY, SURVEYS OF BUSINESS CONFIDENCE YIELD VARIED RESULTS. THE BUSINESS COMMUNITY IS MORE CONFIDENT ABOUT ITS LONG-RUN OUTLOOK UNDER THE NEW GOVERNMENT, BUT SURVEYS OF SHORT-TERM EXPECTATIONS INDICATE THAT MOST BUSINESSMEN FEEL THE RECOVERY PROCESS WILL BE SLOW.

9. THE THREE MOST IMPORTANT FACTORS IN THE LONGER-TERM PROSPECT FOR THE GOVERNMENT'S ECONOMIC PROGRAM ARE (1) THE OUTCOME OF THE GOVERNMENT'S EFFORT TO DEAL WITH AUSTRALIAN LABOR ON WAGE MODERATION; (2) THE RATE AT WHICH CONSUMER CONFIDENCE AND DEMAND REVIVE AND (3) EXTERNAL DEVELOPMENTS

WHICH WILL DIRECTLY AFFECT DEMAND (ESPECIALLY JAPANESE) FOR AUSTRALIAN EXPORTS, THEREBY INDIRECTLY INFLUENCING THE PACE OF DOMESTIC INVESTMENT AND BUSINESS ACTIVITY.

10. THE GOVERNMENT APPEARS DETERMINED TO ADJUST DOWNWARD THE FORMULA USED FOR INDEXING WAGES TO QUARTERLY CPI MOVEMENTS. THIS REFLECTS A CORRECT CONVICTION THAT, TAKEN BY ITSELF, THE AUTOMATIC ADJUSTMENT OF WAGES TO KEEP PACE WITH INFLATION SUPPORTS CONTINUED INFLATION. ON THE OTHER HAND, LABOR'S ATTACHMENT TO THE PRINCIPLE OF KEEPING WAGES EVEN WITH, AND PREFERABLY A STEP AHEAD, OF INFLATION, WILL GENERATE BITTER RESISTANCE TO SUCH A CHANGE. MANY OBSERVERS BELIEVE A CHANGE IN THE FORMULA WOULD CAUSE LABOR TO ABANDON INDEXATION AND RESUME SUCCESSFUL EFFORTS TO OBTAIN EVEN LARGER WAGE INCREASES. THIS STRUGGLE PROMISES TO BE A CENTRAL ISSUE OF FUTURE GOVERNMENT-LABOR RELATIONSHIPS. A RELATED ISSUE NOW DEVELOPING IS WHETHER AND HOW RAPIDLY THE GOVERNMENT WILL IMPLEMENT THE 1975 MATHEWS COMMISSION INCOME TAX INDEXATION PROPOSALS (CANBERRA A-109). THE GOVERNMENT IS UNDER PRESSURE TO SPEED UP THE THREE-YEAR PHASE-IN IT NOW UNCLASSIFIED

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CONTEMPLATES. WHILE TAX INDEXATION WOULD GIVE AN IMPORTANT BOOST TO BUSINESS ACTIVITY AND BE HELPFUL IN REDUCING PRESSURE ON WAGE DEMANDS, THE GOVERNMENT IS CONCERNED OVER ITS COUNTER-EFFECT IN RAISING THE DEFICIT.

11. THE FLAT LEVEL OF CONSUMER DEMAND IS ACCOMPANIED BY AN HISTORICALLY HIGH LEVEL OF PERSONAL SAVINGS. THIS LEVEL IS GENERALLY ATTRIBUTED TO UNEASINESS OVER HIGH UNEMPLOYMENT. AT THIS TIME THERE IS NOT FIRM EVIDENCE THAT CONSUMER DEMAND IS REVIVING.

12. EXPORT PROSPECTS ARE DAMPENED BY THE EXPECTATION OF FLATTENING OR CUTBACK IN JAPANESE MINERAL DEMAND. THE AGRICULTURAL EXPORT OUTLOOK, ESPECIALLY FOR BEEF AND WOOL, APPEARS BRIGHTER. INDUSTRIAL EXPORTS, SERIOUSLY UNDERMINED BY RISING AUSTRALIAN PRODUCTION COSTS, HAVE A POOR OUTLOOK BUT ARE RELATIVELY UNIMPORTANT IN THE TOTAL AUSTRALIAN ECONOMY.

13. COLLECTIVELY, THESE FACTORS OFFER NO BASIS FOR ASSUMING RAPID IMPROVEMENT EITHER ON INFLATION OR IN BUSINESS ACTIVITY AND EMPLOYMENT. THE MOST OPTIMISTIC PROSPECT IS THAT THROUGH CONTINUED WAGE, AND POSSIBLY TAX, INDEXATION THE INFLATIONARY PRESSURE OF WAGES CAN BE MODERATED WHILE OVERALL BUSINESS ACTIVITY SLOWLY RECOVERS. IF, ON THE OTHER HAND, GOVERNMENT'S EFFORTS PRODUCE WIDE INDUSTRIAL UNREST, THE ATTENDANT PRODUCTION DISRUPTION AND LARGER WAGE INCREASES TO THE STRONGER UNIONS COULD PROLONG THE HIGH INFLATION RATE

WHICH IS GENERALLY AGREED TO BE AT THE ROOT OF AUSTRALIA'S SEVERE ECONOMIC DIFFICULTY.

14. BROADLY VIEWED, THE NEW GOA ECONOMIC APPROACH AND STRATEGY APPEAR SOUND. THERE IS INEVITABLY ROOM FOR DIFFERENCES OF JUDGEMENT RESPECTING QUESTIONS OF DEGREE OR EMPHASIS. THE VALUE OF SOME MARGINAL EXPENDITURE CUTS IN RELATION TO THE EFFECT OF SUCH CUTS ON CONFIDENCE, THE SEVERITY OF MONETARY POLICY, AND DETAILED TACTICS RESPECTING WAGE POLICY, IMPORT PROTECTION AND TRADE PRACTICES ARE EXAMPLES OF SUCH QUESTIONS. BUT THE MAIN ELEMENTS OF THE STRATEGY APPEAR SOUNDLY CONCEIVED, AND THE PROSPECT THAT ITS SUCCESS MAY BE SLOW AT BEST AND UNCERTAIN AT WORST REFLECTS THE UNCLASSIFIED

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MAGNITUDE OF THE ECONOMIC PROBLEM AUSTRALIA FACES AS WELL AS ITS VULNERABILITY TO WORLD ECONOMIC FORCES, RATHER THAN ANY FUNDAMENTAL DEFECT IN THE STRATEGY ITSELF.
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